

Better safe than sorry: Time to prepare for a ‘no deal scenario’

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At the October EU Summit, as expected, the EU27 did not conclude that the Brexit negotiations had progressed sufficiently to warrant opening the discussions on the future (economic) relationship between the UK and the EU. The main sticking point continues to be the UK's financial obligations with a lack of concreteness to the apparent offer made by Prime Minister May in her Florence speech, as well as indications that some member states see this offer as way below what is required. Another outstanding issue concerns the role of the European Court of Justice in the post-Brexit era, in particular whether it is needed to uphold EU citizens' rights.

The delay is problematic, not least because the clock is ticking and little time remains to find agreement on all the issues on the table – financial obligations, rights of EU citizens residing in the UK, the Irish border, a transition agreement, as well as the framework for future EU-UK relations – and then to ratify it. The earliest we can now expect to move to the second phase in the negotiations is at the next EU Summit in December. This will only happen if there are further concessions from Prime Minister May, most crucially on the final bill the UK is willing to accept.

Progress nevertheless?

Despite deciding not to move onto the next phase in the negotiations, European leaders acknowledged that there had been progress in the UK position, expressing confidence that sufficient progress will be reached by December. Many see Theresa May's Florence speech as a significant step forward, not only for acknowledging (some) financial obligations, but also for recognising that an “implementation period” will be necessary to ensure an orderly transition into the long-term relationship. Consequently, EU27 leaders decided to start considering among themselves what the future relationship between the EU and the UK could look like, in preparation for December.

But this might be an overly optimistic interpretation of how much further Prime Minister May can go. The opposition within her own party continues to be a challenge. It demands, for example, that the UK should not accept any new EU legislation during the transition period or that money should only be paid for market access but not for the legacy costs related to EU membership. Furthermore, it insists on exiting the Single Market and the Customs Union despite the severe economic and political consequences this entails, including with regard to the situation in Northern Ireland. The voices which call for her to walk away from the talks are growing louder, vowing that no deal is better than a bad deal.

The real conflict is yet to come

It is an open question whether Theresa May actually wants such a deal given its potential to split the Conservative Party and spell the end of her political career. Even if she manages to conclude and push through a divorce agreement, this would only be a first step. The framework for the long-term relationship would still have to be decided in the course of the withdrawal negotiations.

This is much trickier than both sides have acknowledged so far. From a domestic UK perspective, there is no majority for any version of a post-Brexit relationship. All of the existing arrangements, for example, Canada, Switzerland, Norway, or Ukraine, have significant disadvantages. At the heart of the UK's difficulty is a fundamental dilemma: a soft Brexit would

minimise economic harm but entail making political concessions that are not acceptable to Brexit supporters. A hard Brexit would cause a significant level of economic harm and thus have political consequences. This is why the 'have-the-cake-and-eat-it' model – benefits of the Single Market without the associated obligations – is still in the debate, despite having been categorically ruled out by the EU27 from the beginning.

The danger is that the UK might never be politically ready to accept this fundamental trade-off. If this is the case, the cliff edge looms, whether at the end of the Article 50 period in March 2019 or at the end of any transition deal. This ultra-hard, chaotic Brexit – no deal entails an absence of a legal framework for cross-border exchange and thus a seize-up of any cross-border activity – might happen either by default if the process simply runs out of time or by design if Theresa May decides that she can benefit politically from walking out of the talks.

Such a no deal scenario is hugely damaging to the UK, while also imposing a significant cost on the EU27. But it is fuelled by those who claim (mistakenly) that this is simply some form of falling back on WTO rules or those who believe that even a high cost is worth it as long as it creates an irreversible Brexit. A no deal will create gridlock at the UK's ports and airports and will shift legal risks to citizens and businesses. But the fallout will only be experienced too late, after the UK has crashed out.

Even if there is a continuation of negotiations in good faith, it seems unlikely that the UK can accept second class membership – inside the Single Market and Customs Union but with all obligations and no political rights. This is not the position of either the Conservatives or Labour. But equally a free trade deal will be hard to negotiate. Such a deal offers no gains from trade to be distributed but rather costs from disintegration to be allocated across the economy.

What can the EU27 do?

Given the volatility of UK politics and its related high degree of uncertainty, the EU27 should not make any assumptions about what might or might not become possible politically in the UK with regard to the post-Brexit relationship. Instead, there is a need to work out 'blueprints' under different scenarios, which would be ready for implementation whenever a political compromise is found in the UK.

The EU27 must also prepare for a no deal scenario. There needs to be greater consideration of what a 'no deal' deal would entail: what are the critical decisions and investments that need to be taken to ensure that even in a no deal scenario people and goods can still move across the border, especially in Northern Ireland where otherwise the political crisis would resurface.

No deal is the outcome that everyone fears given the huge costs it would impose, especially on the UK but also on the EU27. But despite the tentative progress we have recently witnessed, a no deal scenario remains the most likely outcome, given the significant political divisions in the UK and London's fundamental dilemma: an economically acceptable deal is politically unacceptable while what is politically acceptable falls a long way short of the current economic status quo, being inside the Single Market and the Customs Union.

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